

Directors and officers liability insurance: A deep dive on bribery and corruption

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Introduction

International regulatory landscape

In recent years, there has been heightened media focus on the prevalence of bribery and corruption activities both domestically and internationally. Companies found to be involved in bribery and corruption are facing prosecution as well as intense public scrutiny.

Regulators around the world are increasingly engaging in collaborative efforts and information sharing in an effort to apply greater scrutiny on corporate and individual conduct. This worldwide effort aims to support and facilitate the prosecution for unethical behaviour and promote responsible business practices.

Australia strengthens anti-bribery laws

Notably, Australia is taking steps to strengthen anti-bribery laws, which had previously been criticised as being largely ineffective and under-enforced.

The National Anti-Corruption Commission was established in Australia in November 2022 and commenced operations in July 2023. Since its inception last year, it has already conducted numerous investigations and has overseen a number of successful convictions.

The Australian Government has a zero-tolerance approach to bribery and corruption.¹

On 29 February 2024, the *Crimes Legislation Amendment (Combatting Foreign Bribery) Bill 2023* (the Bill) passed the Senate. The Bill creates a new 'absolute liability' offence of 'failing to prevent bribery of a foreign official' by an 'associate'.² Significant penalties attach to the new offence, namely:

- the greater of: A\$31.3 million or 3 times the benefit received, or
- if the court cannot determine the benefit's value: 10% of the corporate group's annual turnover.

These changes will commence on 9 September 2024, six months after the Bill received royal assent. Following similar amendments in the UK in 2010, there was a significant uptick in the number of prosecutions brought for foreign bribery.³

This changing landscape and heightened focus make it ever more critical that companies put in place procedures to identify bribery and corruption risks. They must also implement systems to address those risks and discourage illegal behaviour.

This whitepaper explores the extent of cover available under a directors and officers (D&O) liability insurance policy in relation to a bribery and corruption event – from investigation to prosecution to fines and penalties.

What is 'absolute liability'?



Absolute liability means that the crime is committed in the absence of proof of intention or fault by the corporation. A corporation is deemed to have committed the offence if an 'associate' commits the bribery offence for the profit or gain of the corporation, unless the corporation can prove that it has adopted adequate procedures to prevent bribery.⁴

What is an 'associate'?

Under the Bill, an associate is broadly defined to include an employee, contractor, agent, subsidiary or controlled entity of the corporation, or a person that otherwise performs services on behalf of the corporation.

Please note that whether or not, and to what extent, a particular allegation of bribery and corruption and the related losses are covered depends on the specific facts and circumstances of the loss and the terms and conditions of the insurance policy as issued. It is impossible to state in the abstract whether the policy will provide coverage in any given situation.

¹ www.austrade.gov.au/en/how-we-can-help-you/programs-and-services/bribery-of-foreign-public-officials

² A similar provision is found under section 7 of the *UK Bribery Act*.

³ *Seven years in the making: Australia's Foreign Bribery Law amendments pass parliament*, 4 March 2024, Abigail Gill and Joshua Aird, Corrs Chambers Westgarth

⁴ *New 'Failure to prevent Bribery' Offence before Australian Parliament*, July 2023, Abigail McGregor and Hoory Yeldizian, Norton Rose Fulbright

D&O policy structure

Coverage type	Party insured	Scope of cover
Side A D&O cover	The directors and officers	Covers the directors and officers for personal liability and associated legal costs and expenses in circumstances where the company is prohibited or unable to pay these costs.
Side B Company reimbursement cover	The company	Covers a company where it can and does indemnify or defend its directors and officers.
Side C Securities entity cover	The company	Covers a company but only for claims made by shareholders in relation to its shares.

- Traditionally, a D&O policy provided coverage under two categories (insuring clauses) – Side A and Side B.
- Both sides A&B of cover apply only to **loss incurred by the directors and officers in claims made against the directors and officers**. Neither insures loss incurred by the company for claims made against the company.
- Side B only reimburses the company for amounts it pays on behalf of its D&O policy under indemnity arrangements.
- Many D&O policies now include a third insuring clause (Side C), which insures **loss incurred by the company, resulting from certain types of claims, for the company's own wrongful acts**, even if directors and officers are not named as defendants.

Worldwide exposures

Corrupt conduct is a global issue. For organisations with international operations, a single bribery event can result in multiple offences under different jurisdictions. As many anti-bribery and corruption laws apply in Australia and overseas, individuals and corporations can be prosecuted whether the offence occurred here or abroad, with many anti-bribery laws having extensive extraterritorial reach.

Consequently, to ensure bribery and corruption exposures are as adequately protected as possible, organisations should strongly consider D&O policies with worldwide cover.

Cover for investigations into corrupt conduct

As investigations into bribery or corruption can result in adverse findings and lead to civil or criminal proceedings against directors or officers, it is important that provision for coverage of the associated legal costs is included in a D&O policy.

Most D&O policies offer some cover for legal costs incurred by directors and officers in preparing for, responding to, or attending a formal investigation. While sub-limits may apply, the better policies provide this cover up to the full policy limit, even when a wrongful act has not yet been alleged and contain an advance payment promise. This is important as many investigations are conducted more as an evidence-gathering exercise, particularly at the preliminary stage.

However, cover is not readily available for legal costs incurred by a *company* who is the subject of an investigation. Limited exceptions apply.

Pre-investigations

Some D&O policies provide cover for costs incurred by directors or officers in preparing formal notifications to regulators or official bodies of an actual or suspected material breach of a company's legal duty.

Similarly, directors or officers might incur costs for conducting internal investigations if requested by a regulator, following a formal notification of bribery and corruption. Some D&O policies may also cover these costs.

Market-leading policies will include cover for internal inquiries conducted by a company, as well as raids or on-site visits by an official body such as a regulator. This cover may be sub-limited and additional premium and conditions may apply.

Adverse investigatory outcomes

The consequences of any type of investigation into corrupt conduct can vary. In more severe cases, an investigation can lead to:

- criminal prosecutions against the company and its directors and officers,
- fines and penalties against the company and its directors and officers,
- the extradition, disqualification or imprisonment of directors or officers,
- follow-on civil proceedings,
- significant legal costs and expenses,
- disgorgement of profits,
- damage to reputation and brand, and
- disruption to business.

Are prosecutions, civil penalty proceedings, disqualification orders and extradition proceedings for corrupt practices covered?

1. Prosecutions

If a prosecution is commenced against directors and officers, this should trigger the definition of a 'claim' in the better D&O policies as it typically includes criminal proceedings.

As a result, the insurance policy should cover directors and officers for amounts they become legally liable for in defending a prosecution.⁵ This will typically be subject to the application of the 'dishonesty' exclusion and the exclusion for 'matters uninsurable at law'.

Importantly, a D&O policy should typically allow for the payment of defence costs to be advanced prior to the final disposition of any criminal prosecution.

However, it is important to note that if it is determined a director or officer is *not* entitled to cover (including through the application of any exclusion), most D&O policies include provisions which requires the insured to repay any defence costs advanced back to the insurer.

Prosecutions against the company itself may not be covered as the definition of 'securities claim' in some D&O policies does not include criminal proceedings against the company.

2. Civil penalty proceedings

The definition of 'claim' in most D&O policies should allow cover for any civil penalty proceedings instigated by a regulator against a director or officer for statutory breaches following an investigation.

3. Disqualifications and extradition proceedings

Most D&O policies provide some cover for legal costs and expenses incurred in defending disqualification orders. The better D&O policies will also cover costs allowing a director or officer to bring proceedings to challenge an order disqualifying them from holding office as a consequence of a 'claim' or regulatory investigation.

Most D&O policies will also provide cover for extradition proceedings.

⁵ Refer to the definition of 'Loss' under your D&O policy, taking note of any exclusionary language.

Fines and penalties

Although some D&O policies expressly exclude cover for fines or penalties (in particular, criminal fines and penalties on public policy grounds), the better policies provide worldwide cover for civil fines and pecuniary penalties.

Market-leading policy wordings cover fines or penalties including those resulting from strict liability offences, provided that the fine or penalty is not derived from a wilful, deliberate or intentional act.

Further, some D&O policies have been endorsed so the definition of 'loss' includes cover for civil penalties assessed against an insured person, pursuant to the *Foreign Corrupt Practices Act* (FCPA).

Ex turpi causa maxim

Ex turpi causa is a common law principle whereby no action can arise from your own illegal act or morally reprehensible acts.⁶ Notwithstanding express cover as outlined above, most, if not all, D&O policies (typically by virtue of the definition of 'loss') exclude '*matters uninsurable at law*' or '*amounts the insurer is legally prohibited from paying by law or regulation*' (with the better ones qualifying this to '*the jurisdiction in which the claim is determined*'). This is for reasons of public policy on the basis that people should not benefit from their own wrongdoings or be indemnified against the consequences of wrongdoings. The availability of an indemnity in such cases would undermine the deterrent impact of the fine or penalty. Any insurance contract that insures against these risks would be void and unenforceable. This would include any policy that claims to indemnify a person against criminal liability if the crime can only be committed with guilty intent.

Strict liability

The position is less clear where the crime is one of strict liability and the offender is morally innocent. Although debatable, general consensus in the legal and insurance industries appear to be that an indemnity can be given in this scenario. The outcome may depend on whether there is an element of fault or intent attributable to the person who has committed the strict liability offence or the express language of the legislative provision in question, if any.

The test of whether a fine or penalty is in fact 'insurable at law' can be uncertain. In some cases, it may be absolutely clear (for example, amendments to the *Work Health and Safety Act (2011) NSW* making it an offence to inter alia arrange/provide insurance or give an indemnity for a monetary penalty under that Act).⁷ In other cases, it may not be so clear and jurisdictional issues as well as legislative and judicial interpretation will come into play.⁸ In recent years, courts have made non-indemnification orders based on implied powers arising out of legislative provisions that impose penalties designed to deter conduct to give effect to that purpose.

Cover for fines and penalties under a D&O policy will also be limited by the application of the 'dishonesty' exclusion which will exclude cover for any fine or penalty arising out of any 'deliberately fraudulent act or omission', 'wilful conduct' or 'wilful breach of duty'.

Finally, a D&O policy does not usually provide cover for fines and penalties assessed against a company itself.

Disgorgement of profits

Disgorgement of profits as a remedy for corrupt conduct tends to be more applicable to companies than to directors and officers. Consequently, companies are unlikely to be afforded cover under a D&O policy, even in the context of a securities claim. This is due to the 'dishonesty' exclusion, which is triggered when a company gains any profit, remuneration or advantage to which it was not entitled.

In other cases, the definition of 'loss' under a D&O policy will expressly exclude 'any amount representing a profit or advantage to which the corporation was not legally entitled'.

Restrictions on coverage for disgorgement orders are not uncommon in D&O insurance based, in part, on the legal principle of unjust enrichment.

⁶ See *Safeway Stores Ltd v Twigger*.

⁷ Similar provisions can be found in *Work Health and Safety* legislation in Western Australia and Victoria. However, this restriction does not apply to legal costs incurred in defending such proceedings.

⁸ Refer to Marsh's [Insurability of Fines and Penalties](#) whitepaper.

Are follow-on civil lawsuits based on violations of anti-bribery laws covered?

Civil lawsuits are captured by the definition of 'claim' in all D&O policies.

The high-profile, large quantum follow-on civil lawsuits based on violation of anti-bribery laws generally take two forms. They are either:

- securities class action lawsuits filed by company shareholders (for example, alleging that FCPA investigations into corrupt conduct caused the company's share price to fall), or
- in the form of a shareholder derivative lawsuit, filed on behalf of the company itself.

Some D&O insurers offer cover for shareholder derivative suits.

The definitions of 'claim' and 'loss' in a typical D&O policy may be broad enough to trigger cover for a company under Side C coverage, and for directors and officers of a company under Side A coverage for the above referenced lawsuits. However, cover for the resulting losses may be compromised by the 'dishonesty' exclusion and the exclusion for matters uninsurable. The 'USA Insured versus Insured' exclusion may also impact a shareholder's derivative lawsuit unless one of the exceptions apply.

Public relations expenses

The better D&O policies will cover reasonable costs and charges of hiring a public relations firm to mitigate the effects of any reputational damage from investigations or litigation into corrupt practices.

Impact of the 'dishonesty' exclusion

D&O policies are not intended to provide cover for claims arising from dishonest or fraudulent acts, or wilful or intentional breaches of law. Accordingly, if a director or officer has wilfully engaged in bribery or other corrupt conduct, any resulting loss such as a fine or penalty is unlikely to be covered.

A 'dishonesty' exclusion in the better D&O policies will not apply to defence costs advanced under the D&O policy until a final non-appealable adjudication, or in some cases, a written admission is reached. This policy wording language is what really makes a D&O policy worthwhile in the context of claims *alleging* corrupt conduct. It provides the directors and officers some level of protection and makes it more difficult for an insurer to decline cover for legal costs when directors and officers need them most.

Notwithstanding that costs advanced may need to be repaid to the insurer if the director or officer is ultimately found to have engaged in dishonest or fraudulent conduct (hence triggering the 'dishonesty' exclusion), having cover for the advancement of defence costs can be invaluable in supporting the insured through legal proceedings or the trial process.

Other relevant exclusions

Some D&O policies expressly exclude claims arising under the ***UK Bribery Act and Foreign Corrupt Practices Act***.

Most if not all policies exclude '**matters uninsurable at law**' or 'loss the insurer is prohibited from paying at law.' Claims where there is a judicial finding of corrupt conduct will likely fall within these. It's questionable whether express exclusions in this regard are required in any event.

Some D&O policies now also include '**sanctions' exclusions**, which restricts coverage that would expose insurers to any sanction, prohibition or restriction under United Nations resolutions or the trade or economic sanctions, laws or regulations of specified jurisdictions.

Cover for retired directors and officers

Most D&O policies provide cover for former directors and officers, typically under the definition of ‘insured person’, with two important caveats:

- First, cover for former directors and officers is only for claims related to events occurring *before* the director or officer left the company and that relate to the individual’s capacity as a director or officer of the company.
- Second, cover for former directors and officers typically continues only to the extent the company continues to purchase D&O insurance in the future, with limited exceptions.

The better D&O policies offer a ‘retired directors and officers extension’ of cover. The definition of ‘retired insured person’ varies amongst different policies.

The extension typically provides that if the D&O policy is not renewed or replaced when the policy expires, any retired insured person may be granted a further period in which to notify claims. This is typically 84 months (seven years). This extension is not available in certain circumstances, notably in the event of a transaction or insolvency.

Duty of disclosure

In Australia, an insurer is only entitled to avoid a contract of insurance if an insured is fraudulent, although a court may disregard avoidance in certain circumstances.⁹

Alternatively, insurers can reduce their liability (in some case to nil) as a result of any fraudulent non-disclosure of fraudulent misrepresentation by the insured.¹⁰ This can come into play during the insurance renewal process where the insured would typically complete an insurance proposal form, which would include material disclosures on various aspects of the insured’s business activities and exposures.

This is a real risk for insureds in the context of claims alleging bribery and corruption. Some questions and considerations include:

- Was corrupt conduct known at policy inception, and if so, by whom?
- Whose knowledge is relevant for the purposes of the proposal form?
- Is the proposal form construed as a separate proposal for each insured?
- Will the failure of one insured to comply with the duty of disclosure be imputed on other insureds?

The better D&O policies would say no to the last question. The best policies contain a provision that specifies the policy will not be rescinded or avoided for any reason. It is important to read your policy wording carefully and have a sound understanding of the various provisions and terms of coverage.

Culture of corruption

Investigations into certain organisations, both domestically and abroad, indicate that the rule of law is often being disregarded where a culture of corruption is rife.

In recent years, regulators in Australia and abroad have heightened their focus and intentions to pursue companies and their officers for corporate governance breaches and misconduct. To minimise this exposure, directors must develop appropriate controls and implement robust compliance systems to manage corrupt conduct within their organisation. This framework should include *‘appropriate channels for reporting suspected breaches of the law and that individuals who do report breaches are protected from persecution within the company.’*¹¹

⁹ As per section 28 of the *Insurance Contracts Act 1984* (ICA), subject to section 31 of the ICA.

¹⁰ As per section 28(3) of the ICA.

¹¹ www.ag.gov.au/crime/foreign-bribery/foreign-bribery-offences-and-penalties

Strengthening risk management frameworks

Systems and controls failing to effectively tackle bribery and corruption continues to be a challenge for directors and organisations. As regulators and legislators worldwide intensify their scrutiny of corrupt conduct and engage in more internationally co-ordinated investigations, it is paramount for organisations to have a thorough understanding of the associated risks and deploy effective strategies for managing bribery and corruption which cascades through all levels of the organisation and its business operations.

While a D&O policy is designed to protect the personal liabilities and assets of directors and officers, it may not always respond to a bribery and corruption event in the manner expected. Cover for the company itself is even more precarious due to the serious nature of the conduct in question and the fact that it is against public policy for unlawful and dishonest conduct to gain any monetary benefits or be protected by an insurance policy.

For companies looking to protect their directors, officers, business and reputation from such misconduct, the priority lies in ensuring appropriate risk management frameworks are in place to detect, respond to and prevent corruption, while also fostering a culture of compliance and responsible business practices.



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